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SUBJECT: NEW FINANCE LAW MIXES PROTECTIONISM AND FITFUL PROGRESS

REF: ALGIERS 848

¶1. SUMMARY: The 2008 supplemental finance law adopted on July 27 raised the per-barrel oil price used to calculate government revenue and included measures to stimulate business growth and develop the country's moribund agricultural sector. At the same time, the law alienated many with a controversial new car tax designed to fund public transportation projects. Expenditures for the remainder of 2008 include measures aimed at promoting local and rural development; boosting the agricultural, construction and tourism sectors through tax incentives and subsidies; and supporting low-income workers and disabled persons. The new per-barrel benchmark for oil is USD 37, replacing a USD 19 standard that had skewed budget calculations and produced massive budget surpluses as the price of oil skyrocketed. The car tax, affecting all new vehicles, has caused much consternation in the press and among ordinary Algerians, who see it as another undue financial hardship that strikes at the common person rather than the rich. END SUMMARY.

OIL REFERENCE PRICE PUSHES UPWARD

¶2. The 2008 supplemental budget, referred to as the Complementary Finance Law, was approved by the Council of Ministers on July 27. It reset the petroleum export reference price from USD 19 to USD 37 per barrel of oil. The USD 19 reference had been used to estimate government income since 2000 (nearly 98 percent of Algeria's export income comes from hydrocarbons sales), which skewed the country's budgets as the price of oil has skyrocketed in recent years. The new reference price increased estimated government receipts by 44 percent to USD 42 billion, and total expenditures were increased by 13 percent to USD 68 billion. Almost USD 2 billion of capital expenditures will be allocated for a dairy subsidy and for rural development and electrification projects. The USD 30 billion budget deficit will be covered by an effective stabilization fund where revenues are deposited after calculating the difference between market oil price and the budget reference price. In presenting the draft law, the finance minister projected that Algeria's economic growth would reach 3 percent in 2008, with 6.5 percent growth outside of the hydrocarbons sector. He estimated inflation for 2008 would rise one-half of a point to 3.5 percent, and that exports would be valued at USD 30 billion.

PLANTING THE SEEDS FOR DOMESTIC AGRIBUSINESS

¶3. In what the government described as an effort to respond

to the worldwide food crisis, the supplemental budget contained measures aimed at promoting domestic agriculture production. The value added tax (VAT) will be waived for the purchase of seeds, fertilizers and phytosanitary products through 2009, and the leasing of agricultural equipment produced in Algeria will be exempt from VAT for the next 10 years. In addition, the government will reorganize the current subsidy mechanism and create a new fund to help small farmers. The new law also revised the agricultural production regulation fund, which provides price supports to farmers to absorb weather risks in an effort to buffer the consumer food market from price shocks.

GIVING WHAT YOU GET

¶4. To spur project investment, corporate taxes for industries such as construction, public works and tourism were reduced. However, in a move that was announced after the release of the finance law, Algerian tax law was amended to require companies that receive investment tax incentives to re-invest the value of those tax breaks within four years. Companies that fail to re-invest their tax benefits will be forced to repay the value of the incentives, plus a 30-percent penalty.

NEW TAXES ON NEW CARS

¶5. The most controversial provision of the supplemental budget was an additional tax on new cars, which in Algeria means imported cars. The consumer tax ranges from USD 760 to

USD 2285, depending on the type of car and the fuel it uses. Car dealers will pay an additional one-percent tax that will be used to develop public transportation systems. The independent media have assailed the new car tax in the weeks since its announcement, speculating that dealers will only pass their tax burden on to consumers. Louisa Hanoune, head of the Trotskyist Workers Party, publicly criticized the new car tax, lamenting the negative impact it would have on the ordinary Algerians, especially those in rural communities that lack public transportation. Algerians complain that the measure further erodes their purchasing power, and will increase the country's reliance on used, higher-polluting and less safe vehicles.

COMMENT: WHERE IS ECONOMIC REFORM HEADED?

¶6. The mix of increased agricultural subsidies, taxes on new cars, and the requirement that tax incentives be reinvested relatively quickly may signal a new spirit of protectionism within the Algerian government, or at least a further circumscription of the limited economic liberalization undertaken since 2002. Other new taxes on real estate, when coupled with the president's public admission that his economic policies, especially in the area of privatization and investment promotion, have failed (reftel) and a more recent policy statement by the new prime minister that future foreign investments in Algeria will require a majority stake held by an Algerian partner (septel), may signal a growing element of nationalism in the government's economic policy. But if the idea was to appeal to ordinary Algerians by placing new requirements on foreign companies seeking to do business here, it didn't work: any public approval was quickly offset by the negative reaction to the car tax.
DAUGHTON